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UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
SAN FERNANDO VALLEY DIVISION

In re

CYNTHIA LYNN HERRERA AND
MANNY REY HERRERA III

Debtor

Case No. SV 03-18130-GM

Chapter No. 7

**MEMORANDUM OF OPINION
REGARDING TRUSTEE'S FINAL
REPORT AND APPLICATION FOR
APPROVAL OF PROFESSIONAL FEES
AND EXPENSES**

Date: FEBRUARY 16, 2005

Time: 10:00 A.M.

Place: Courtroom 303

21041 Burbank Blvd.

Woodland Hills, CA 91367

Debtors filed a joint petition on October 2, 2003, showing personal property of under \$20,000, virtually all of it claimed as exempt. The trustee [Brad Krasnoff] did not object to the exemptions. The debtors' schedules revealed a residence worth \$360,000 on which there were liens of \$252,000+. Debtors claimed \$75,000 of the equity as exempt [no objection by the trustee as to this amount], leaving approximately \$23,000 of non-exempt equity for the estate, without reduction for costs of sale. At the time of filing, Southern California was in an upwardly spiraling real estate market.

The §341(a) meeting was on November 7, 2003 and on November 14 the holder of the second trust deed filed a motion for relief from the automatic stay, immediately followed by the trustee's application to employ his own firm as counsel. On December 8, the moving party withdrew the Motion for Relief from the Automatic Stay and shortly thereafter the trustee (through application and order prepared by his counsel) employed a real estate broker to sell the house. He has employed his own firm as counsel. On February 20, 2004, trustee's counsel filed

1 a motion to sell the house for \$445,000, with an overbid procedure. Proper notices were given
2 by counsel and after an auction in court (conducted by counsel without the trustee's presence)
3 the house was sold to an overbidder for \$487,000. Escrow closed in mid-April. Thereafter
4 certain claims were withdrawn and the final report was prepared. This was a straight-forward
5 case with no unusual issues. It was handled expeditiously by all concerned.

6 A review of the time records for the attorney for the trustee and those of the trustee
7 shows that this case was run as one might handle a small business. The trustee was the manager,
8 who had three "staff" members working for him: his assistant for trustee work ["JM"], and two
9 attorneys. On the "case management side," JM prepared the final report but did not review bank
10 statements or prepare reports for the Office of the United States Trustee. Those duties were done
11 by Mr. Krasnoff.

12 On the "property management and sale side," there was a senior attorney (Amy Goldman,
13 whose time is valued by the firm at \$375 per hour) and a junior attorney (Han Lee, who was
14 admitted to the bar in 2002 and whose time is valued by the firm at \$125 per hour). Once the
15 trustee realized that there was equity for the estate in this house, he turned the work over to Ms.
16 Goldman and Mr. Lee. Ms. Goldman was very efficient in her coordination of this case, with
17 Mr. Lee doing most of the negotiation and legal work. This was a simple sale of an asset and
18 while that involved quite a few steps, they were not complex and there is no indication in the
19 applications or court documents that this sale was in any way out of the ordinary.

20 The trustee served as the owner/manager of this little business. Periodically Mr. Lee or
21 Ms. Goldman would bring him up to date or have him review some papers and then sign them.
22 But they did the legal work on this case. The only part of the trustee's time that could need the
23 expertise of a bankruptcy professional was his conduct of the 341(a) meeting [1 hour]¹ and his
24 review of claims [2.10 hours total]. The rest of the time he served as the business manager.

25 The trustee filed his final report and request for compensation which stated that his
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27 ¹ Though it seems impossible that a case that his this straightforward required 1 hour for
28 the 341(a) examination, I am accepting Mr. Krasnoff's representation that it did.

1 trustee “business” had spent 26.2 hours on this case [22.7 hours of his own work and 3.5 hours
2 by JM]. The application for fees by the firm for the legal work done accounted for an additional
3 48 hours totaling \$7,500, mostly dealing with a sale of the residence.

4 The maximum fee under 11 USC § 326(a)² for the trustee would be \$23,888, but the
5 trustee notes on his report that he is seeking \$18,500, which represents a voluntary reduction of
6 \$5,888 from the statutory cap. If the trustee’s time were to be compensated based on his hourly
7 rate as an attorney, the full amount of the award would be approximately \$9,200 (22.6 hours of
8 attorney work by Mr. Krasnoff at \$390 per hours and 3.5 hours by his assistant at \$100 per
9 hour).³ While the trustee has done a good job, as has his attorney, the request of \$18,500, equates
10 to over \$700 per hour for the 26.2 hours accounted for, which is almost twice the billing rate that
11 Krasnoff commands for work that he does as an attorney. This request requires me to analyze
12 the factors that I must consider in awarding compensation to a trustee. While I don’t think that it
13 is particularly relevant, I do note that in this case there are 8 unsecured creditors totaling
14 \$109,500 and the payout will be 77% if the trustee receives \$18,500. If the trustee receives
15 \$9,200, the payout to unsecureds would increase to about 91%. All of the unsecured creditors
16 are financial institutions (credit card debt).

17 At the hearing on February 16, 2005, Mr. Krasnoff gave a cogent and compelling
18 argument that the appropriate way to calculate his fees would be to start at the statutory cap and
19 then reduce the fee if the work was not competently done. He supported this position with a set
20 of business facts and figures, which included the following:

21 1. Mr. Krasnoff stated that he receives about \$180,000 per year total for all of his work
22 as a trustee. He personally spends about 1,000 hours per year being a trustee, so this averages
23 about \$180 per hour, which is well below his normal hourly rate for his legal practice. From this
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25
26 ² Unless otherwise noted, all sections referred to are in 11 United States Code, §101 et.
27 seq.

28 ³ In preparing the tentative ruling I calculated a total of \$9,825 by using a presumed
billing rate of \$375 per hour (based on that of Ms. Goldman) for all 26.2 hours.

1 amount he must pay overhead expenses, including the salary of his administrator and the
2 administrator's assistant (which is shared with another trustee in the firm). These staff expenses
3 take about half of what he brings in as a trustee.

4 2. Mr. Krasnoff commented that the recap of work done on this case does not include
5 time for the court appearance, distribution of assets, and other actions necessary to close the
6 case.

7 3. Mr. Krasnoff argued that the court should begin with the cap in order to allow the
8 trustees to make-up for losses that they suffer on other cases. He asserted that the fee ceiling is
9 there to limit the amount that the trustee can make-up on any single case.

10 4. Mr. Krasnoff asked why a trustee should be treated any differently from a real estate
11 broker or a contingency attorney. It is standard and accepted practice to pay those professionals
12 a percent of what they bring into the estate, so why should a trustee be held to a different
13 standard? Particularly, argued Krasnoff, these other professionals can pick their cases, while
14 trustees can't; the debtor picks its creditors, the trustee doesn't.

15 5. Mr. Krasnoff noted that trustees create estates. Sometimes they create something
16 from nothing, as often the schedules show that there are no assets to be liquidated and
17 distributed. In these cases, if the trustee is not diligent, there will be nothing to distribute to
18 creditors.

19 The basic issue that I must decide is whether Congress intended that the trustee be able to
20 spread his costs of doing business over his entire caseload so that there would be little
21 relationship between the actual work done in any given case to the fees allotted to the trustee on
22 that case, particularly if such a compensation scheme is required to entice high-quality
23 professionals to serve as trustees. Or am I directed to view each case as a self-contained entity,
24 with fair compensation to the trustee for the work done in that particular case without regard to
25 the economics of the trustee system under the current law. I believe that it is the latter.

26 While there are more than a handful of cases which address this issue, I have found no
27 dispositive decision in the Ninth Circuit. But the Tenth Circuit opinion in In re Miniscribe
28

1 Corporation⁴ is persuasive, supporting the following statutory analysis:

2 1. The percentage amounts described in §326(a)⁵ are not a starting point for calculating
3 the reasonable fee, but they are a limitation on the upper amount that the court can award.

4 2. As required in §326(a), the court may only grant reasonable compensation in the
5 amount calculated under §330.

6 3. §330(a)⁶ connects “reasonable compensation” to the “actual, necessary services”
7 rendered by the trustee and does not tie it to the success or failure of those services [though the
8 amount available for payment may exist only because of the trustee’s success in recovering and
9 liquidating property of the estate].

10 4. §330(a)(3)⁷ lists the elements to consider “in determining the amount of reasonable
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12 ⁴ 309 F.3d 1234 (10th Cir. 2002).

13 ⁵ §326(a) reads as follows: “In a case under chapter 7 or 11, the court may allow
14 reasonable compensation under section 330 of this title of the trustee for the trustee’s services,
15 payable after the trustee renders such services, not to exceed 25 percent on the first \$5,000 or
16 less, 10 percent on any amount in excess of \$5,000 but not in excess of \$50,000, 5 percent on
17 any amount in excess of \$50,000 but not in excess of \$1,000,000, and reasonable compensation
18 not to exceed 3 percent of such moneys in excess of \$1,000,000, upon all moneys disbursed or
turned over in the case by the trustee to parties in interest, excluding the debtor, but including
holders of secured claims.”

19 ⁶ §330(a)(1) reads as follows: “After notice to the parties in interest and the United States
20 Trustee and a hearing, and subject to sections 326, 328, and 329, the court may award to a
21 trustee, an examiner, a professional person employed under section 327 or 1103-- (A) reasonable
22 compensation for actual, necessary services rendered by the trustee, examiner, professional
person, or attorney and by any paraprofessional person employed by any such person; and (B)
reimbursement for actual, necessary expenses.”

23 ⁷ §330(a)(3)(A) reads as follows” “In determining the amount of reasonable
24 compensation to be awarded, the court shall consider the nature, the extent, and the value of such
25 services, taking into account all relevant factors, including--(A) the time spent on such services;
26 (B) the rates charged for such services; (C) whether the services were necessary to the
27 administration of, or beneficial at the time at which the service was rendered toward the
28 completion of, a case under this title; (D) whether the services were performed within a
reasonable amount of time commensurate with the complexity, importance, and nature of the
problem, issue, or task addressed; and (E) whether the compensation is reasonable based on the
customary compensation charged by comparably skilled practitioners in cases other than cases

1 compensation to be awarded.” First of all the court must look at the nature, extent, and value⁸ of
2 the services. In doing so, the court is to review all relevant factors including [but not limited to]
3 the time spent on the services; the rates charged for the services; whether these services were
4 necessary or beneficial at the time that they were performed; whether the time spent on
5 performance was reasonable given the complexity, nature, and importance of the task; and
6 “whether the compensation is reasonable based on the customary compensation charged by
7 comparably skilled practitioners in cases other than cases under this title.” These are many of
8 the basic factors used in Johnson v. Georgia Highway Express, Inc.⁹ This analysis must be done
9 on a case-by-case basis and without regard to the economics of the trustee system as a whole.

10 5. Once the court has calculated the reasonable compensation as described in §330(a)(3),
11 the amount is tested against the cap set forth in §326(a). If it exceeds the cap, it must be reduced
12 to the maximum allowed under the percentage formula.

13 Virtually all opinions have determined that it is inappropriate for the court to base
14 trustee’s fees on the §326(a) cap. The stalking horse for the other viewpoint is In re Guyana
15 Development Corporation¹⁰, which has been roundly criticized. Guyana asserts that the trustee
16 can be compared to a contingency attorney who creates a common fund and is therefore entitled
17 to compensation in the form of a percentage of what he created. Although the judge in Guyana
18 attempts to use the legislative history to support this contention, she does so incorrectly, as
19 discussed below. The other viewpoint is expressed in In re Marvel Entertainment Group, Inc.,¹¹

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21 under this title.”

22 ⁸ How should the value be considered? Does it apply to the creditors of this particular
23 estate or to the whole system? Case authority - based largely on the lodestar methodology -
24 seems to focus on the concept of what these same services would cost on the open market. They
25 only deal with value to the specific creditors or the system in terms of a possible enhancement
(aka “bonus) above that market value.

26 ⁹ 488 F.2d 714 (5th Cir. 1974).

27 ¹⁰ 201 B.R. 462 (Bankr. S.D. Tex. 1996).

28 ¹¹ 234 B.R. 21 (D.Del. 1999).

1 which attacks Guyana on both legal and policy grounds.

2 These two cases were reviewed by the Tenth Circuit in Miniscribe Corporation, which
3 holds that percentage-based compensation is unavailable. The fee is to be calculated using the
4 lodestar test, with appropriate enhancements under Johnson and - because some work is
5 managerial and some is more professional - the court should determine a uniform blended hourly
6 rate that applies to the number of hours spent by the trustee.

7 Mr. Krasnoff's arguments concerning the business-side of being a trustee are not new.
8 They were known to the Bankruptcy Commission of 1970, which was concerned about the
9 concept that the creditors of a more lucrative estate would end up paying a higher percent of
10 their recovery than those of a less flush one. Under the Bankruptcy Act as it existed prior to
11 1978, liquidating trustees received \$10 per case and

12 such sum as the court may allow, but in no event to exceed [a percentage scale is
13 set forth]. . . *Provided, however*, That if in any case, after the trustee has paid all
14 expenses of administration and has realized upon all available assets, the
15 maximum compensation allowable to him hereunder does not exceed \$150, the
16 court may of its own motion allow the trustee a fee which with the commissions,
17 if any, paid or to be paid him, shall not exceed \$150.¹²

18 In reviewing this provision, the Bankruptcy Commission stated that as "so often happens,
19 maximums tend to become minimums. In all but the largest cases, trustees receive the maximum
20 fee. This is especially true with respect to the \$150 discretionary fee."¹³

21 The Commission went on to state that the
22 existence of the \$150 discretionary fee and of nominal asset cases is based on an
23 averaging rationale. In every case, the trustee receives \$10 for his services from
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25 ¹² Bankruptcy Act §48c(1). Italics in original.

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27 ¹³ Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc.
28 No. 93-137, 93d. Cong., 1st Sess., Part I (1973), p. 93 [reprinted in Collier's App. Pt. 4(d)(i), p. 1181].

1 the \$50 statutory filing fee for the case. It is clear that \$10 is inadequate to
2 compensate a trustee for the paper shuffling that must be done in even the
3 simplest non-asset case. Trustees are willing to take no-asset cases with only a
4 \$10 fee, however, because through tacit agreement with the bankruptcy judges
5 that appoint them, they know that they will receive the \$150 fee in any case where
6 there are adequate assets to pay it, even though the reasonable value of the
7 trustee's services in such a case may be far less than \$150. Thus, in the long run,
8 the trustees average out their fees, with the creditors in nominal asset cases
9 subsidizing trustee for all cases.¹⁴

10 After five years of legislative hearings, debates, and analysis, the Bankruptcy Act of 1978
11 [referred to as the Bankruptcy Code] was passed by the House of Representatives [HR 8200]
12 with the companion bill in the Senate designated as S 2266. Each bill was accompanied by a
13 section by section analysis and the House report also contained a detailed narrative stating
14 legislative intent.¹⁵

15 The House Report stated that the bill changes the fee structure by increasing the
16 percentage payable in the lower range. "However, the discretionary \$150 fee is eliminated. Its
17 use today bears no relationship to the services performed in the cases in which it is awarded.
18 Instead, its use represents the averaging theory of fees, which is unjustified in a bankruptcy
19 system that is supposed to operate for the benefit of creditors on a case-by-case basis."¹⁶ Later
20 when the House Report gives a section-by-section analysis, it notes under §326 that it
21 must be emphasized that this section does not authorize compensation of trustees.

23 ¹⁴ Id. at 94 (Colliers 1181). Emphasis added.

24 ¹⁵ Report of the Committee on the Judiciary, House of Representatives, to Accompany
25 H.R. 8200, H.R. Rep. No. 95-595, 95th Cong., 1st Sess. (1977), reproduced in Colliers App. Pt.
26 4(d)(i), pp. 1047-1726.13. [Herein House Report.] Report of the Committee on the Judiciary,
27 United States Senate, to accompany S.2266, S. Rep. No. 95-989, 95th Cong., 2d Sess. (1978),
reproduced in Colliers App. Pt. 4(e)(i), pp. 1927-2144.7. [Herein Senate Report.]

28 ¹⁶ House Report p. 103-4, Colliers 4-1192. Emphasis added.

1 This section simply fixes the maximum compensation of a trustee. Proposed 11
2 U.S.C. 330 authorizes and fixes the standard of compensation. Under section 48c
3 of current law, the maximum limits have tended to become minimums in many
4 cases. This section is not intended to be so interpreted. The limits in this section,
5 together with the limitations found in section 330, are to be applied as outer
6 limits, and not as grants or entitlements to the maximum fees specified.¹⁷

7 It is absolutely clear that Congress did not intend to support the trustee system by an
8 across-the-board tax on straightforward lucrative estates. Unfortunately, Guyana focuses only
9 on the concept that Congress intended to create an incentive to trustees to search out and recover
10 assets and fails to note that Congress focuses this on a case-by-case basis and rejects the theory
11 of a common-fund for all bankruptcy cases.¹⁸

12 But having said that, Mr. Krasnoff raises some very real issues about the economics of
13 the trustee system. I do not have the expertise to suggest solutions (although as noted below,
14 Congress is in the process of enacting changes), particularly as the Bankruptcy Act of 1978
15 specifically intended judges to divorce themselves from the administration of cases and thus
16 created the Office of the United States Trustee [or in two districts that of Estate Administrator].
17 I will only comment that it is critical to the system that the panel of trustees be as professional as
18 possible and that it is my experience that all current members of the panel from the San Fernando
19 Valley division qualify as professional and capable trustees.

20 But I am required to enforce the law as written and not I might wish it to be. Thus, in
21 calculating the appropriate fee for Mr. Krasnoff, I must start with the quantity, quality, and
22 difficulty of the work that he actually did, taking into consideration the customary charges for
23 similar work by comparably skilled practitioners outside the bankruptcy arena. Who might those
24 practitioners be? What is the market value of the services provided by the trustee in a chapter 7
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26 ¹⁷ Id. at p. 327, Colliers 4-1455. The identical language is found in the Senate Report, p.
27 37, Colliers 4-1973.

28 ¹⁸ 201 B.R. at 475.

1 case?

2 I have little evidence to make comparisons, but the most analogous “business” that I can
3 think of is that headed by a chapter 13 trustee. Both types of trustees have to handle large sums
4 of money, must deal with the courts on a regular basis, must be fully versed in the bankruptcy
5 laws, and handle some cases which give large rewards and many others which provide little or
6 nothing. Both preside at §341(a) meetings, object to improper claims of exemptions, and file a
7 variety of forms and notices with the court. Both are subject to appointment, removal, and some
8 level of oversight by the Office of the United States Trustee. Both are subject to the fluctuations
9 in case filings. Both can have their caseloads reduced or expanded as the OUST increases or
10 decreases the number of trustees in their district or division.

11 There are, of course, differences. The chapter 13 trustee is more regulated as to the
12 number of her staff and her salary is fixed by law. The chapter 7 trustee has more litigation
13 (such as preference and fraudulent transfer actions, though he often hires counsel to handle
14 these). The chapter 7 trustee is more likely to object to claims, while the debtors do this in most
15 chapter 13 situations. The chapter 13 trustee is able to group her court appearances in a much
16 more efficient way than can the chapter 7 trustee. The chapter 7 trustee often (and in this district
17 always) operates the trustee business as a part-time rather than full-time occupation, while the
18 chapter 13 trustees in this district are all full-time in that capacity. These are only a few of the
19 differences.

20 But the issue is what is the customary charge for similar work by comparably skilled
21 practitioners. While the chapter 13 trustees are certainly within the bankruptcy arena, they are of
22 high quality and could be earning at least as much outside the area of bankruptcy. And though
23 some have a business background, other chapter 13 trustees are attorneys. So I feel that this is a
24 fair comparison.

25 The maximum salary of a full-time chapter 13 trustee is set by law and it can be reduced
26 if there are not enough cases to justify that amount. The chapter 13 trustee is paid solely through
27 fees that she collects. Once she has paid her staff and other operating expenses (which are
28 approved or at least reviewed by the United States Trustee), then she can pay herself (to the

1 extent that there is money left over) up to a maximum of \$165,000 gross. She has no other
2 compensation or benefits and this is before-tax dollars.

3 Mr. Krasnoff stated that he grosses about \$180,000 for trustee work, which takes about
4 half of his time (2000 hours per year is not unrealistic for a full-time lawyer and Mr. Krasnoff
5 devotes 1000 of those hours to his trustee work). He also reported that after paying his staff and
6 trustee expenses, he is left with about \$90,000. Thus, he would be grossing about \$180,000 per
7 year for himself (from which he must pay his own pension, taxes, and benefits) if he were a full-
8 time chapter 7 trustee. This is not out-of-line with the compensation of a full-time chapter 13
9 trustee. This would mean an hourly rate of \$180 is a reasonable rate for running the trustee
10 business, which is exactly what Mr. Krasnoff makes for his trustee work.

11 So in doing the required analysis of reasonableness, I cannot apply the hourly rate of Mr.
12 Krasnoff as an attorney [\$390/hour], but must use that of Mr. Krasnoff as a businessman
13 [\$180/hour]. Given this analysis, I do not believe that a blended rate is appropriate, since that
14 starts with the concept that the trustee is a lawyer or accountant and is billing his client for his
15 work on an hourly basis, with some work properly done by paraprofessional and other work
16 requiring the expertise of professionals with various levels of skill and experience. The trustee is
17 really running a business in which he is entitled to the profit after payment of all expenses.

18 While it would be appropriate for me to reduce the award to about \$5,000, it has become
19 the custom to use an hourly rate for the trustee that is equivalent to his fee when he works as a
20 lawyer and I see no reason to disturb that at this time, particularly given the coming change in
21 the law. And because I granted an interim order that the trustee could disburse \$9,825 to himself
22 [based on an hourly rate of \$375] and because no party objected to the higher amount requested
23 by the trustee, I will allow the amount of \$9,825 although I have grounds to reduce it further. As
24 noted in In re Computer Learning Centers, Inc.,¹⁹ in many chapter 7 cases the trustee is paid the
25 cap - not because this is an entitlement, but in recognition that in smaller cases the value of the
26 services is at least the amount of the cap. While that does not apply here, the efficient running of
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28 ¹⁹ 285 B.R. 191, 230 (Bankr. E.D. VA 2002).

1 this case does appear to have saved the estate enough to justify using a professional hourly rate
2 for the trustee, who remained actively involved in the decision-making even in areas where
3 counsel did the actual work.

4 A note about the future. The new bankruptcy bill which is winding its way through
5 Congress and will likely become the law during 2005 makes a change in the trustee
6 compensation section. If it is passed without amendment, §330(a) will now have a new subpart
7 (7), which will read: “(7) In determining the amount of reasonable compensation to be awarded
8 to a trustee, the court shall treat such compensation as a commission, based on section 326.”
9 This appears to be a clumsy attempt to make the cap into a set commission and create a
10 presumption that it is the reasonable amount, subject to the other considerations set forth in
11 §330(a)(3).²⁰ If so, that will be the law of the future. But I must deal with the law as it now
12 stands.

13 For the above reasons, the trustee’s fees will be approved in the amount of \$9,825.

14
15 MARCH 24, 2005

/s/

GERALDINE MUND
United States Bankruptcy Judge

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24 _____
25 ²⁰ If this is the intent of Congress, it is ironic that they have done a 180 degree turn from
26 the “evil” found by the Bankruptcy Commission of 1970 and the House and Senate in 1977-8
27 that judges were too close to the trustees whom they appointed and used a fee enhancement to
28 satisfy those trustees, even though this put a burden on the creditors in other cases. In the case
before me the OUST supports the concept of an enhanced fee for exactly the same reasons that
the Commission and Congress excoriated judges in the 1970s. Hmmm!

CERTIFICATE OF MAILING

I, Kathleen Ogier, a regularly appointed and qualified clerk of the United States Bankruptcy Court for the Central District of California, do hereby certify that in the performance of my duties as such clerk, I personally mailed to each of the parties listed below, at the addresses set opposite their respective names, a copy of the

MEMORANDUM OF OPINION REGARDING TRUSTEE'S FINAL REPORT AND APPLICATION FOR APPROVAL OF PROFESSIONAL FEES AND EXPENSES

in the within matter. That said envelope containing said copy was deposited by me in a regular United States mailbox in the City of Los Angeles, in said District, on

3-24-05

Cynthia and Manny Herrera - Debtors

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Kathleen Ogier

(Clerk)